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SUPREME COURT OF THE UNITED STATES

NO. 28

STATE OF TEXAS and J. C. CLOPTON and BULLOCK HYDE, RECEIVERS, ETC.,
Petitioners,

vs.

DAVID DONOGHUE, TRUSTEE OF TRINITY REFINING COMPANY, DEBTOR,
Respondent.

MOTION FOR REHEARING BY DAVID DONOGHUE, TRUSTEE UNDER AN ORDER TO LIQUIDATE, RESPONDENT

[redacted]

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To the Honorable the Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

Now comes David Donoghue, Trustee under an order to liquidate the estate of the above named debtor, and files this his petition for rehearing and as grounds therefor respectfully shows the following:

I

The controversy between the State of Texas and this Trustee, as representative of the creditors, is not as to the right of the State to maintain an action for forfeiture but concerns the substantive results of a judgment enforcing forfeiture as to the oil which is admittedly in the lawful possession of the Trustee.

The bankruptcy court recognized this fact and denied the State permission to proceed in the state court not because of the *nature* of the contemplated action by the State but because *the State could obtain all relief in the bankruptcy court which it could ultimately obtain if it should obtain a judgment enforcing a forfeiture of the oil in a state court.*

We respectfully submit that the bankruptcy court was correct and that the action in denying the State leave to institute a suit enforcing a forfeiture in a state court *did not deny the State its day in court.*

The very gist and basis of an action by the State to enforce a forfeiture involves two issues: (a) was the oil in controversy produced as allowable oil? (b) if not, when does or did title pass to the State? On such issues, if the State of Texas should be permitted to institute an action in a state court, the state court might enter any one of four judgments, namely: (1) the oil is allowable oil and no recovery by the State; (2) the oil was illegally produced and title vests in the State at the date of judgment; (3)

the oil was illegally produced and title vests in the State at the date of judgment, but relates back to the date of production; (4) the oil was illegally produced and title vested in the State at date of production.

If the state court should enter judgment (1) admittedly the State of Texas would have no right to the oil.

If the state court should enter judgments (2) or (3) the State of Texas would then file its motion in the bankruptcy court for a surrender of the oil. That motion would be contested by this Trustee upon the basis of 57(j) of the Bankruptcy Act, which is applicable to proceedings under 77B (subsection k) and bars judgments for forfeiture as well as claims for forfeiture. *In re: Abramson and Fichhandler* (C. C. 2nd Cir.), 210 Fed. 878; *United States v. Birmingham Trust Company* (C. C. 5th Cir.), 258 Fed. 562; *in re: Southern Steel Co.* (S. Ct. Ala.), 183 Fed. 498. Thus there would ultimately be presented to the bankruptcy court for determination the question as to whether or not Section 57(j), of the Bankruptcy Act, bars a recovery by the State.

If the state court should enter judgment (4), then, as is stated in the majority opinion, the bankruptcy court, on motion by the State, would doubtless recognize that title and direct the Trustee to hand over the oil, or to account for it, to the State.

Thus, irrespective of the character of the judgment which might be entered by the state court, the ultimate recovery by the State depends *solely upon the question of title.*

It is a general rule of substantive law not limited to bankruptcy matters that

> "Where a court of competent jurisdiction takes possession of property through its officers this withdraws it from the jurisdiction of all other courts, which though of concurrent jurisdiction may not disturb that possession; and *that the court originally acquiring possession is competent to hear and determine all questions respecting title, possession and control of the property.*"

Isaacs v. Hobbs Tie & Timber Co., 282 U. S. 734, 737, 75 L. Ed. 645, 664; *In re: Baldwin*, 291 U. S. 610, 616, 78 L. Ed. 1020, 1023; *Murphy v. Hoffman*, 211 U. S. 562, 568, 53 L. Ed. 327; *Board of Trade v. Johnson*, 264 U. S. 1, 11, 68 L. Ed. 533; *Herbert v. Crawford*, 228 U. S. 203, 205, 57 L. Ed. 800.

That this Trustee lawfully took possession of the oil in controversy and now holds rightful possession was determined by final judgment of the Circuit Court in this case and affirmed by the opinion of this Court. It follows that under the general rule the bankruptcy court had and has jurisdiction to determine all questions concerning *title, possession and control* of such oil.

If the order of the bankruptcy court denying the State permission to proceed in a state court to enforce a forfeiture is sustained and the State urges its alleged right to the oil in the 77B proceedings issues (a) and (b) above will, just as they would in an action in the state court, constitute the gist of the State's right of action.

If the bankruptcy court should enter judgment (1) above admittedly the State would have no right to the oil.

If the bankruptcy court should rule in accordance with judgments (2) and (3) above as to the vesting of title, at the same time it would determine whether or not 57(j) of the Bankruptcy Act bars a recovery of the oil by the State.

If the bankruptcy court should rule in accordance with judgment (4) above, then, as is stated in the majority opinion, it would doubtless recognize that title in the State and direct the Trustee to hand over the oil or account for it to the State.

Accordingly, whether the State urges its position in a state court or in the bankruptcy court, the ultimate result will be the same. This being true it is submitted that the order of the bankruptcy court denying the State permission to proceed in a state court was not an abuse of discretion.

The principles governing the exercise of judicial discretion have been defined by this Court as "the

court * * * is to be guided by considerations that under the law make for the ascertainment of what is just for the claimants, the debtor and the estate," *Faust v. Munson*, S. S. Lines, No. 19 decided November 9, 1936, 299 U. S. 71, 81 L. Ed. 30, "* * * is directed by the reason and conscience of the judge to a just result * * *," *Langes v. Green*, 282 U. S. 531, 541, 75 L. Ed. 520, 526, "* * * implies conscientious judgment * * *," *The Styria v. Morgan*, 186 U. S. 1, 9, 46 L. Ed. 1027, 1033.

Any analysis of the inevitable results of reversing or affirming the order of the trial judge denying the State of Texas permission to proceed in a state court entails the following considerations: if reversed, (a) the exclusive jurisdiction of the bankruptcy court provided in 77B (a) as the means of eliminating the evils of equity receiverships is undermined; (b), a final determination of the instant case must await the pleasure of the State in obtaining judgment in a state court; (c), if, assuming an appeal, after the case has passed the state district court, the court of civil appeals and the supreme court of Texas, the judgment as finally determined is of type (2) or (3) above, under standard practice three years will have passed and the ultimate controversy between the parties will still depend upon a final adjudication concerning 57(j) by the federal courts; and (d), the multiplicity of suits and the attendant delay and expense will constitute an unfair and unjust burden on the civil creditors.

In contrast, if the decision of the trial judge is affirmed (a) the State of Texas will obtain the same relief which it could have ultimately obtained if it had obtained judgment in the state court, (b) the entire controversy will be determined in one action with a minimum expenditure of time and expense to all parties.

In view of the foregoing, we respectfully submit that the order of the trial judge in all things fully met the test of what constitutes a valid exercise of judicial discretion.

II

It is the Trustee's sincere opinion that Section 77B of the Bankruptcy Act is one of the most splendid instruments devised in the history of jurisprudence for the administration of financially embarrassed organizations. The evils of ancillary receiverships, the bargaining strength of selfish minorities and lack of control over the plan of reorganization, counsel fees and future attacks, all have been eliminated by Section 77B. The strength and effectiveness of 77B in a large measure arises from the increased jurisdiction granted the bankruptcy courts by subsection (a) and other provisions of the section. Accordingly, while not controlling here, we respectfully submit that the statement in the majority opinion "The State's right to bring the suit in the state court is the same as if on its vol-

untary petition the company had been adjudged bankrupt on the day its petition for reorganization was approved. Section 77B (o)," is error and in the future may be made the basis of attempts to encroach upon the powers of bankruptcy courts which are essential to an effectuation of the purposes of 77B. Subsection (o) of 77B is not a limitation upon jurisdiction, but is an additional grant of powers and jurisdiction to the bankruptcy courts. The first two phrases in subsection (o) read, "In proceedings under this section *and consistent with the provisions thereof* * * *." In subsection (a) the bankruptcy courts are granted "exclusive jurisdiction of the debtor and his property wherever located." By subsection (c) (10) the bankruptcy court is authorized to "enjoin or stay the commencement or continuation of suits against the debtor * * *." By reason of these and other provisions of Section 77B, the powers and jurisdiction of a bankruptcy court in a proceeding under 77B have been held to be far greater than the powers and jurisdiction of the same court in an ordinary bankruptcy. *Continental Illinois Nat. Bank & Trust Co. v. Chicago, Rock Island & Pac. Ry. Co.*, 294 U. S. 648; *In re: Prudence Bonds Corp.* (C. C. 2nd Cir.), 75 F. (2d) 262, (summary jurisdiction without right of possession); *In re: Cloisters Bldg. Corp.* (C. C. 7th Cir.), 79 F. (2d) 694, (power to grant stays); *In re: Greyling Realty Corp.* (C. C. 2nd Cir.), 74 F. (2d) 734, (extraterritorial authority);

In re: O'Brien, 78 F. (2d) 715, (exclusive jurisdiction over debtor).

By reason of the authority granted the bankruptcy courts by subsections (a) and (c) (10) of 77B, and the powers emanating from the actual possession of the Trustee, which powers and authority are not limited by 77B (o), the trial court had jurisdiction to hear and determine all controversies concerning the oil. The State has no "right" under 77B (o) to maintain its action in a state court, for exclusive jurisdiction is in the bankruptcy court. If justice required, on motion by the State, the bankruptcy court might waive its exclusive jurisdiction to the extent of permitting an action in the state court. Then the authority of the State would be derived not from 77B (o) or other grant of right in 77B but upon the permission granted by the bankruptcy court.

III

In conclusion, if we look to the substance and not to the form of the State's position in this case, we find that the mantle of righteous crusading it has vigorously waved in the circuit court and this court hides a purpose wh ch a court of equity would not further. The debtor is insolvent and an order of liquidation has been entered. The State admits that it seeks the oil merely as a penalty against the debtor, yet in what possible way would the debtor be penal-

ized through a recovery by the State? If the State recovers, the oil will be sold as under ordinary execution and the State will deposit the funds "to the credit of the General Revenue Fund of the State of Texas." The result is that while the debtor will not be penalized the State will be unjustly enriched at the expense of civil creditors.

Congress by the enactment of 57(j) intended that the creditors at large shall "not be mulcted" by penalties and forfeitures accruing to a State.

In this case the equities, the intent of Congress as to the exclusive jurisdiction of a bankruptcy court and the considered opinion of the trial judge all support the denial of permission to the State to proceed in a state court. Only injustice, established beyond question, should afford a sufficient predicate for overruling such considerations. *Smith v. Vulcan Iron Works*, 165 U. S. 518, 526; *New York v. Irving Trust Co.*, 288 U. S. 329, 333:

> "The Federal government possesses supreme power in respect to bankruptcies. International Shoe Co. v. Pinkers, 278 U. S. 261, 265. If a state desires to participate in the assets of a bankrupt, she must submit to appropriate requirements by the controlling power; otherwise, orderly and expeditious proceedings would be impossible and a fundamental purpose of the Bankruptcy Act would be frustrated."

We respectfully submit that in justice to all parties at interest the decision of the trial court should

be affirmed. It is, accordingly, prayed that this petition for rehearing be granted and that upon further hearing herein the decision of the circuit court be in all things affirmed.

DAVID DONOGHUE, Trustee, Under
Order to Liquidate,

By R W Kellough
Attorney.

R. W. KELLOUGH,
Tulsa, Oklahoma;
H. T. MCGOWN,
H. L. LOGAN, JR.,
Fort Worth, Texas,
Of Counsel.

David Donoghue, trustee in reorganization, through his attorney, W. B. Harrell, joins in the above petition.

DAVID DONOGHUE,
Trustee in Reorganization,
By W. B. Harrell, Attorney.

I, R. W. KELLOUGH, duly appointed attorney for David Donoghue, Trustee, under order to liquidate, hereby certify that this petition is presented in good faith and not for delay and that copies of this petition have been mailed to counsel for petitioners and to counsel for the original respondent in this case.

R W Kellough

SWORN TO AND SUBSCRIBED before me this 22 day of December, A. D. 1937.

Bernice Simmons

Notary Public in and for Tarrant County, Texas.

SUPREME COURT OF THE UNITED STATES.

No. 28.—October Term, 1937.

State of Texas and J. C. Clopton and Bullock Hyder, Receivers, etc., Petitioners,
vs.
David Donoghue, Trustee.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

[December 6, 1937.]

Mr. Justice Butler delivered the opinion of the Court.

This writ is limited to the questions raised on the application of Texas to the United States court for the northern district of that State in a proceeding under § 77B of the Bankruptcy Act [1] for permission to institute proceedings in a state court for the confiscation of oil held by the trustee but claimed by the State as "unlawful oil" because produced or transported in violation of state conservation measures.

Texas statutes [2] and orders of its Railroad Commission purport to prorate production of crude oil, to prohibit purchase, transportation or handling of that produced in whole or in part in excess of the amount allowed,[3] to impose fines and penalties for violations,[4] and to make oil produced or transported in violation of statute or order subject to confiscation in an action brought by the State for that purpose.[5] The statute declares that if at the trial it shall be

[1] 11 U. S. C., § 207.

[2] Texas Revised Civil Statutes, 1925, Title 102.

[3] Art. 6049e, § 10.

[4] Art. 6036.

[5] Art. 6066 (a), § 10:

(a) "All unlawful oil . . . [is] hereby declared to be a nuisance and shall be forfeited to the State as hereinafter provided. . . .

(b) "When the Attorney General is advised from any source of the presence and existence of unlawful oil . . . it shall be his duty to institute a suit in rem against such unlawful oil . . . and against all persons owning, claiming or in possession thereof, such suit to be brought in the name of the State . . . in any court of competent jurisdiction in Travis County or in the county in which such oil . . . is located. If it shall appear to the court . . . that unlawful oil . . . mentioned in the petition . . . [is] in danger of being removed, wasted, lost or destroyed, the court is authorized and required . . . to issue restraining orders or injunctive relief . . .

found that the oil is unlawful, the court shall render judgment forfeiting the same to the State and authorizing an order directed to sheriff or constable commanding him "to seize and sell" the condemned oil. Costs of suit and expenses of the sale are to be paid out of money received from the oil, and the balance becomes part of the general revenue fund of the State.

There is before us no question as to validity of the State's measures to regulate production, or as to when, if ever, the oil in controversy became forfeit.[6] The sole issue is whether the bankruptcy court should have permitted the State to bring suit in a state court to have the oil adjudged confiscate.

These are the facts.

Texas sued the Trinity Refining Company in the district court, 126th judicial district, Travis county, to recover fines and penalties for violation of the conservation laws. The court appointed Clopton and Hyder receivers of defendant's property pending the trial of the case. They took possession of property claimed by the defendant, including a large quantity of oil which the State insists had already become its property because unlawfully produced or transported. Later, the State sued the company in the district court, 98th judicial district of the same county, to recover delinquent taxes. That suit having been transferred to the district in which the first was pending, the court there appointed as receivers in the second case the same persons it had appointed in the first one.

Within four months after commencement of the first suit, the company filed its petition in the United States district court, submitting a plan of reorganization. The court found the petition to have been presented in good faith, approved it as properly filed, appointed Donoghue trustee of the debtor, directed him to take

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or to appoint a receiver to take charge of the oil . . . in question, or to direct the sheriff of the county . . . to seize and impound the same until further orders of the court."

(c) " . . . If, upon the trial of such suit the oil . . . in controversy is found to be unlawful . . . then the court . . . shall render judgment forfeiting the same to the State . . . and authorizing the issuance of an order of sale directed to the sheriff or any constable of the county where the oil or products are located commanding such officer to seize and sell said property in the same manner as personal property is sold under execution . . . The money realized from the sale . . . shall be applied, first, to the payment of the costs of suit and expenses incident to the sale . . . and all funds then remaining, shall be . . . placed to the credit of the General Revenue Fund of the State. . . ."

[6] United States *v.* 1960 Bags of Coffee, 8 Cranch 398. See also Clark *v.* Protection Insurance Co., 1 Story (C. C.) 109, 134.

possession of its property, ordered that all persons having property of the debtor deliver it to him and issued in usual form a restraining order preventing interference with his possession or control. The trustee took from the receivers property claimed by the debtor including the oil in question, approximately 77,000 barrels. Texas applied to the bankruptcy court for permission to bring suit in a state court to obtain judgment of confiscation against that oil. The court withheld consent and directed the trustee to retain the oil. The Circuit Court of Appeals sustained that ruling, 88 F. (2d) 48, 51, and to review its judgment upon that issue, we brought the case here. 301 U. S. —.[7]

The State's right to bring the suit in the state court is the same as if on its voluntary petition the company had been adjudged bankrupt on the day its petition for reorganization was approved. § 77B (o). Forfeiture of unlawful oil under Texas law is a penalty imposed to vindicate the State's policy of conservation. *Champlin Rfg. Co.* v. *Commission,* 286 U. S. 210, 240-241. The bankruptcy court exercises jurisdiction under sovereignty that is independent of and foreign to that of Texas. *Moore* v. *Mitchell,* 281 U. S. 18, 23. It is without power to enforce penalties imposed by the State for violation of its laws. *The Antelope,* 10 Wheat. 66, 123. *Wisconsin* v. *Pelican Ins. Co.,* 127 U. S. 265, 289, *et seq.* Cf. § 57 (j), Bankruptcy Act;[8] *New York* v. *Jersawit,* 263 U. S. 493, 496; *United States* v. *Childs,* 266 U. S. 304, 309-310. The State's insistence is not that it is presently entitled to establish a right to forfeit the oil, but that the oil became its property when produced or transported contrary to law. It seeks not to forfeit but to enforce the forfeiture that resulted, as it maintains, immediately from unlawful production or transportation.

Possession or control of the oil by the state court is not essential to its jurisdiction to entertain the suit proposed to be brought.[9] Texas does not claim to be entitled to possession of the oil until final adjudication in the state court. Retention by the trustee is not inconsistent with the maintenance of that suit. He is entitled there

[7] Later, no plan of reorganization having been adopted, the bankruptcy court ordered liquidation of the debtor's property under subds. (c) (8) and (k) of § 77 B. Donoghue was appointed trustee in bankruptcy. § 44; 11 U. S. C., § 72. This Court substituted him in that capacity as respondent in place of himself as trustee of the debtor.

[8] 11 U. S. C., § 93 (j).

[9] Art. 6066a, §§ 10 (b) and (c).

to be heard in support of his claim to the oil. If when the debtor's petition was approved the oil did not belong to Texas, the State was not entitled to have it withheld from the trustee. But, if by reason of unlawful production or transportation, the oil had already by forfeiture become the property of the State, the trustee was not entitled to take or retain it. If in a suit brought by Texas in a state court it should be determined that title to the oil had vested in the State before approval of the debtor's petition, the bankruptcy court doubtlessly will recognize that title and direct the trustee to hand over the oil or account for it to the State. *Rose* v. *Himely*, 4 Cranch 241, 268. *Hudson* v. *Guestier*, 4 Cranch 293, 297. See *Wisconsin* v. *Pelican Ins. Co., supra*, 291.

The filing of the petition for reorganization in the bankruptcy court may not be held to deprive the State of opportunity in its own court to establish its claim that through forfeiture it had already become the owner of the oil for that would be to take the State's property for the benefit of the offending company or its creditors. Nor may the receivers' voluntary surrender of possession to the debtor's trustee prevent adjudication of the State's claim. The bankruptcy court abused its discretion in denying the State's application for permission to institute procedings in the state court and, to the extent that the Circuit Court of Appeals sustained that ruling, its judgment must be reversed.

It is so ordered.

A true copy.

Test:

Clerk, Supreme Court, U. S.

SUPREME COURT OF THE UNITED STATES.

No. 28.—October Term, 1937.

State of Texas, et al., Petitioners,
vs.
David Donoghue, Trustee.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

[December 6, 1937.]

Mr. Justice Cardozo, dissenting.

I think the judgment should be affirmed.

Texas was not the owner of the oil in controversy when it came into the possession of the court of bankruptcy. If she had been such an owner, she could be heard in that court *pro interesse suo*, vindicating her title in reclamation proceedings like any other adverse claimant. By common consent ownership sufficient for such relief was not hers when the court of bankruptcy took the oil into its custody, and is not hers today. "It is not correct to say that property forfeited is vested in the government at the very moment of forfeiture, and the title of the owner immediately devested. On the contrary, the established doctrine is, that, notwithstanding the forfeiture, the property remains in the owner, until it is actually seized by the government, and then by the seizure the title of the government relates back to the time of the forfeiture." *Clark* v. *Protection Insurance Co.*, 1 Story 109, 134; cf. *United States* v. *Stowell*, 133 U. S. 1. So far as I am aware there is no contention to the contrary. The oil "shall be forfeited to the State as hereinafter provided" (Texas Revised Civil Statutes, Art. 6066a, § 10), and not otherwise. The statute does not mean that without the aid of any judgment title is transferred at once on the commission of the offense. The judgment is to be *in rem* and imports control over the *res*. *Pennoyer* v. *Neff*, 95 U. S. 714, 734; *Isaacs* v. *Hobbs Tie & T. Co.*, 282 U. S. 734.

With the oil in the possession of the federal court of bankruptcy—a possession lawfully acquired—leave to sue in the state court for a decree of forfeiture and sale will be an idle and empty form, productive of nothing except delay and vain expense, unless upon the pronouncement of the decree it will be the duty of the court of

bankruptcy to surrender the oil to the court of another jurisdiction, and this for the sole purpose of making a forfeiture effective. I deny that any such duty will exist. Cf. *Isaacs* v. *Hobbs Tie & T. Co., supra.* I find no intimation of its existence in any case till this one. Certainly there is none in the cases now cited in the opinion of the court. True indeed it is that if possession of the *res* were to be acquired by the Texas court at the time of the decree of forfeiture or even at the time of a sale pursuant thereto, a title obtained thereunder would be recognized as valid everywhere. *Wisconsin* v. *Pelican Ins. Co.*, 127 U. S. 265, 291; *Rose* v. *Himely*, 4 Cranch 241; *Hudson* v. *Guestier*, 4 Cranch 293; Dicey, Conflict of Laws, 5th ed., pp. 484, 485. This is far from saying that a court of another jurisdiction which already holds the *res* upon a trust for general creditors will give its possession up in aid of a forfeiture otherwise impossible. "The courts of no country execute the penal laws of another." *The Antelope*, 10 Wheat. 66, 123; *Gwin* v. *Breedlove*, 2 How. 29, 37; *Wisconsin* v. *Pelican Ins. Co., supra; Huntington* v. *Attrill*, 146 U. S. 657, 666; *Loucks* v. *Standard Oil Co.*, 224 N. Y. 99, 102; Dicey, *supra*, p. 212. Cf. Bankruptcy Act, § 57 (j). Within the purview of that doctrine, the state and the federal courts are ranked as courts of separate sovereignties, quite as much as the courts of different states. *Gwin* v. *Breedlove, supra; Moore* v. *Mitchell*, 281 U. S. 18, 23. If the oil in controversy had been removed to California and were in possession of the receivers of a California corporation after a decree of dissolution, would any one contend that the California court would order its receivers to return the property to Texas for the purpose by such return of making a forfeiture effective? A federal court of bankruptcy is subject to no greater duty. The prevailing opinion commits us to a holding that property in one jurisdiction may be diverted from the use of creditors and made to feed a forfeiture in another jurisdiction, a forfeiture *brutum fulmen* unless thus aided from afar. If that is done, the efficacy of penal laws will have taken on a new extension. Without a transfer of possession the forfeiture is dead at birth. A court of bankruptcy will not stir a hand to make it viable.

I am authorized to state that Mr. Justice STONE joins in this opinion.